

**PUBLIC UTILITIES COMMISSION**

505 VAN NESS AVENUE

SAN FRANCISCO, CA 94102-3298

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A2101017

October 28, 2022

Agenda ID #21096**Ratesetting**

TO PARTIES OF RECORD IN APPLICATION 21-01-017:

This is the proposed decision of Administrative Law Judge Hazlyn C. Fortune. Until and unless the Commission hears the item and votes to approve it, the proposed decision has no legal effect. This item may be heard, at the earliest, at the Commission's December 1, 2022, Business Meeting. To confirm when the item will be heard, please see the Business Meeting agenda, which is posted on the Commission's website 10 days before each Business Meeting.

Parties to the proceeding may file comments on the proposed decision as provided in Rule 14.3 of the Commission's Rules of Practice and Procedure.

The Commission may hold a Ratesetting Deliberative Meeting to consider this item in closed session in advance of the Business Meeting at which the item will be heard. In such event, notice of the Ratesetting Deliberative Meeting will appear in the Daily Calendar, which is posted on the Commission's website. If a Ratesetting Deliberative Meeting is scheduled, *ex parte* communications are prohibited pursuant to Rule 8.2(c)(4).

/s/ MICHELLE COOKE

Michelle Cooke

Acting Chief Administrative Law Judge

MLC:mef

Attachment

Decision PROPOSED DECISION OF ALJ FORTUNE (Mailed 10/28/2022)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of San Gabriel Valley
Water Company (U337W) for
Authority to Apply Facilities Fees to
Fund Upgrades to Water Treatment
Facilities in the Fontana Water
Company Division.

Application 21-01-017

**DECISION ADOPTING A SETTLEMENT AGREEMENT,
AUTHORIZING THE USE OF FACILITIES FEES TO OFFSET THE COSTS
FOR PLANT UPGRADES, AND SETTING THE RATE OF INTEREST FOR
ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION AND
POST-IN-SERVICE EXPENSES**

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Attachment A

**DECISION ADOPTING A SETTLEMENT AGREEMENT,
AUTHORIZING THE USE OF FACILITIES FEES TO OFFSET THE COSTS
FOR PLANT UPGRADES, AND SETTING THE RATE OF INTEREST FOR
ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION
AND POST-IN-SERVICE EXPENSES**

Summary

This decision adopts the settlement agreement (Settlement Agreement) between San Gabriel Valley Water Company (San Gabriel) and the Public Advocates Office of the California Public Utilities Commission. In so doing, this decision authorizes San Gabriel, consistent with the Settlement Agreement, to apply facilities fees to offset the costs of planning, designing, and constructing upgrades to water treatment facilities at the Fontana Water Company Division's (Fontana) Sandhill/Summit Treatment Plant (Project). The facilities fees as well as other contributions received to fund the Project upgrades shall be recorded as Contributions in Aid of Construction. The Settlement Agreement is appended to this decision as Attachment A and resolves all issues in this proceeding, except for two, concerning (1) the interest rate for Allowance for Funds Used During Construction and (2) the post-in-service capitalized interest rate.

This decision also resolves the two outstanding disputed issues by setting: (1) the rate of interest for Allowance for Funds Used During Construction at San Gabriel's currently applicable rate for short-term debt; and (2) the post-in-service capitalized interest rate at San Gabriel's currently applicable rate for short-term debt.

All costs associated with the improvements to water treatment facilities in Fontana as part of the Project shall be subject to reasonableness review in San Gabriel's next general rate case. This application is closed.

1. Background

On January 29, 2021, San Gabriel filed the instant Application (A.) 21-01-017 seeking authority to use facilities fees to offset the costs of planning, designing, and constructing upgrades to the Sandhill/Summit Treatment Plant (Project) as part of its Fontana operations.¹ San Gabriel also intends to rename the Sandhill Water Treatment Plant to the Summit Treatment Plant.

The Sandhill Treatment Plant was originally constructed in the 1960s to comply with federal water quality standards by treating and processing local surface water at Lytle Creek.² It currently consists of a diatomaceous earth (DE) filtration facility, a conventional treatment facility, and a hydroelectric generation facility. The hydroelectric generation facility was added in 2013 to reduce the electricity costs of operating the DE and conventional water treatment facilities.³ Decades of use and more rigorous water quality standards prompted San Gabriel to construct the conventional treatment facility in the early 2000s; it was completed and placed into service in 2008.⁴

According to San Gabriel, Fontana's water supply mix is dependent on and vulnerable to fluctuations in surrounding hydrological conditions, groundwater levels, water quality, and impacts from contamination.⁵ San Gabriel asserts that the proposed Project would support meeting current

¹ San Gabriel operates in Los Angeles County and San Bernardino County, producing, treating, storing, distributing, and selling water. San Gabriel has two divisions: the Los Angeles County Division and the Fontana Water Company Division.

² Application of San Gabriel Valley Water Company, January 29, 2021, at 7.

³ *Id.* at 7-9.

⁴ *Id.* at 9.

⁵ *Id.* at 9-10.

customer water demand, vary its water supply sources, and comply with current updated federal and state drinking water standards.⁶

The Public Advocates Office of the California Public Utilities Commission (Cal Advocates) filed a protest to the application on March 3, 2021. San Gabriel filed a response to the protest on March 8, 2021.

On April 29, 2021, a prehearing conference was held. San Gabriel and Cal Advocates (referred to collectively as Parties hereinafter) are the only parties to this proceeding.

On July 12, 2021, the assigned Commissioner issued the Scoping Memo and Ruling (Scoping Memo) in this proceeding. Parties engaged in negotiations between July 13, 2021, through August 26, 2021. A telephonic status conference was held on August 27, 2021. Parties clarified during the August 27, 2021, status conference that they had not reached settlement on all issues in the application and indicated that they wished to continue negotiating.

On August 31, 2021, the Administrative Law Judge (ALJ) issued an e-mail ruling providing directions for evidentiary hearings scheduled to start on September 7, 2021, through September 9, 2021.

On September 7, 2021, Parties met in a continued status conference and developed a revised proposed schedule for the evidentiary hearings. Later in the day on September 7, 2021, Parties informed the ALJ that they had reached a settlement resolving most of the disputed issues in the proceeding. Parties further clarified they agreed to litigate two issues solely through admittance of exhibits and briefing, and therefore the evidentiary hearings scheduled for September 8, 2021, and September 9, 2021, were no longer needed. The ALJ

⁶ *Id.* at 20.

issued a ruling with an updated proceeding schedule on September 8, 2021, accordingly.

On September 27, 2021, Parties filed a joint motion for approval of the Settlement Agreement and a request to move exhibits into evidence. Briefs were filed on October 11, 2021, and Reply Briefs on October 25, 2021, to address the unresolved issues. The record of this proceeding consists of all filed documents and all exhibits as admitted into the record.

On September 23, 2022, the assigned Commissioner issued an Amended Scoping Memo in this proceeding. The Amended Scoping Memo added an additional issue to the scope that was introduced in the Settlement Agreement but had not been included in the initial scoping memo dated July 12, 2021.

2. Settlement Agreement

The Settlement Agreement and its terms and conditions resolve most of the issues scoped in this proceeding and is supported by both parties and in testimony that is part of the record in this proceeding.⁷ Specifically, the Settlement Agreement provides that San Gabriel should be authorized to implement the following:

1. Design, permit,⁸ and construct two new filters, including extension of the existing filter gallery, associated piping, chemical related facilities, and control system upgrades to the Conventional Treatment facility;
2. Decommission and remove the outdated DE filtration facility;
3. Modify Summit's five filters (three existing filters and two newly constructed filters) by replacing the dual media

⁷ Settlement Agreement Between San Gabriel and Cal Advocates, September 27, 2021, at 2.

⁸ Permits for the demolition and removal of the DE facility and other local construction permits.

- (anthracite coal and sand) with granular activated carbon (GAC) under the specified conditions;
4. Modify the Project scope (to include the construction of six GAC contactors, a low lift pumping station, associated piping, and equipment). Permission would be granted by Tier 1 Advice Letter, if DDW⁹ does not approve of the treatment modification presented in item number 3 above;
 5. Submit annual information-only Advice Letters, on or before March 31st of each year, until the Project is completed, so that the Commission, Cal Advocates, Water Division staff, and other interested parties can monitor the Project progress. The Settlement Agreement details what must be included in the annual Advice Letter filing;
 6. Allow for a general rate case (GRC) reasonableness and prudence review; conditions of the review are outlined in the Settlement Agreement. Moreover, San Gabriel commits to exclude the capital costs of the Project from rate base. No Project costs, including Allowance for Funds Used During Construction (AFUDC) and post-in-service capitalized interest related to the Project, will ever be included in San Gabriel's rate base, or become the responsibility of residential customers for ratemaking purposes;
 7. Apply Facilities Fees to fund Summit upgrades. Facilities Fees, as well as any grants or other contributions received to offset the Project costs, shall be recorded as contributions in aid of construction:
 - a. San Gabriel shall record the costs of planning, designing, and constructing the Project in a separate project work order; and
 - b. San Gabriel will offset all such recorded Project costs with the amount of Facilities Fees San Gabriel collects

⁹ Division of Drinking Water (DDW), a part of the California State Water Resources Control Board.

pursuant to Fontana's Tariff Schedule No. FO-FF (Fontana Facilities Fees) until all of the Project costs have been offset and reimbursed; including the cost of San Gabriel's funding of the Project recorded as an allowance for funds used during construction on the unreimbursed balance during construction, if any, and post-in-service capitalized interest on the unreimbursed balance after the Project is completed and placed in service, if any, until all of the Project costs are offset and reimbursed by Facilities Fees.

3. Discussion

3.1. Review of Settlement Agreement

3.1.1. Standard of Review

Pursuant to Rule 12.1(d),¹⁰ parties presenting a settlement agreement have the burden of proof to demonstrate whether the Commission should adopt the Settlement Agreement. Rule 12.1(d) provides:

The Commission will not approve settlements, whether contested or uncontested, unless the settlement is reasonable in light of the whole record, consistent with law, and in the public interest. Proponents of a settlement agreement have the burden of proof of demonstrating that the proposed settlement meets the requirements of Rule 12.1 and should be adopted by the Commission.¹¹

As discussed below, the Commission reviewed the Settlement Agreement and finds that it is reasonable in light of the whole record, consistent with the law, and in the public interest.

¹⁰ All references to the Rule or Rules in this decision refer to the Commission's Rules of Practice and Procedure.

¹¹ Decision (D.) 12-10-019 at 14-15; D.09-11-008 at 6.

3.1.2. Settlement Is Reasonable in Light of the Whole Record

Under the terms of the Settlement Agreement, San Gabriel would design and construct upgrades to the existing water treatment facility, remove the DE filtration facility from the Project assets, and make modifications to the existing filters at the Project to improve the water quality for San Gabriel's customers.

The Settlement Agreement requires San Gabriel to record the costs of planning, designing, and constructing the Project in separate Project work orders and to offset recorded Project costs from facilities fees it collects pursuant to Fontana's Tariff Schedule No. FO-FF.

Other features of the Settlement Agreement allow for ongoing monitoring during the Project through annual advice letters and a GRC reasonableness and prudence review at completion. The ability to amend the scope of the Project after DDW testing and approval was an important component of the Settlement Agreement and a reasonable compromise to control Project costs.

Cal Advocates had raised concerns about the prudence of the costs for the proposed plant upgrades, and the Settlement Agreement makes modifications to the Project that lower costs and includes testing and reporting oversight.

Taken together, these components of the Settlement Agreement settle issues that are within the scope of this proceeding and are reasonable in light of the whole record and should be adopted by the Commission.

3.1.3. Settlement Is Consistent with the Law

On September 27, 2021, San Gabriel and Cal Advocates filed a joint motion to introduce the Settlement Agreement. This filing is compliant with Rule 12.1. The motion contained the required justifications including a statement of factual and legal considerations adequate to advise the Commission of the terms of the

settlement. Parties convened the requisite conference meeting per Rule 12.1(b) with notice and opportunity to participate provided to all parties.

There are no statutory provisions or prior Commission decisions that would be contravened or compromised by the approval of this Settlement Agreement. Therefore, the Settlement Agreement is consistent with the law.

3.1.4. Settlement Is in the Public Interest

As discussed below, the Settlement Agreement is in the public interest. Improved water quality would be achieved through compliance with safe drinking water standards; energy savings will result from decommissioning the DE facility and expanding clean hydro-generation at the conventional facility; and other public health benefits will be attained through reduced levels of total organic compounds (TOC) and elimination of their associated odor.¹²

Furthermore, the Project and the resulting water quality improvements will further the Commission's Environmental and Social Justice (ESJ) goals. In February 2019, the Commission adopted its ESJ Action Plan¹³ as a comprehensive strategy and framework for addressing ESJ issues in each proceeding. Environmental justice means the fair treatment of people of all races, cultures, and incomes with respect to the development, adoption, and enforcement of environmental laws, regulations, and policies.¹⁴

The ESJ Action Plan is focused on disadvantaged communities. Disadvantaged communities refer to the geographic areas throughout California that suffer from a combination of economic, health, and environmental burdens.

¹² San Gabriel Response to E-mail Ruling of Administrative Law Judge Hazlyn Fortune Directing Parties to Address Environmental and Social Justice Issues, June 16, 2021, at 3.

¹³ Environmental and Social Justice Action Plan, Version 1.0, February 21, 2019.

¹⁴ <https://www.cpuc.ca.gov/news-and-updates/newsroom/environmental-and-social-justice-action-plan>.

These burdens include poverty, high unemployment, air and water pollution, and presence of hazardous wastes, as well as high incidence of asthma and heart disease.¹⁵

The City of Fontana is in a region identified by the California Environmental Protection Agency's (CalEPA) CalEnviroScreen mapping tool as being in the 80 to 90 percent category for pollution.¹⁶ This designation identifies the City of Fontana as a disadvantaged community.

The proposed Project improvements to enhance the water quality in this area support ESJ Goal 3. Goal 3 aims to improve access to high-quality water, communications, and transportation services for ESJ communities.¹⁷ Other ESJ goals will be furthered by increased economic activity in the City of Fontana through jobs creation.¹⁸

In addition, the Commission has long acknowledged that, "[t]here is a strong public policy favoring the settlement of disputes to avoid costly and protracted litigation."¹⁹ Consistent therewith, Commission approval of the Settlement Agreement will provide efficient resolution of contested issues. This Settlement Agreement will avoid unnecessary litigation, will provide cost recovery sufficient to enable San Gabriel to continue providing safe and reliable water service to its customers while meeting all applicable water quality standards, and protecting ratepayers from rate increases resulting from

¹⁵ <https://www.cpuc.ca.gov/industries-and-topics/electrical-energy/infrastructure/disadvantaged-communities>.

¹⁶ Response of Cal Advocates to the Ruling Requesting Comment on Environmental and Social Justice Issues, June 16, 2021, at 2.

¹⁷ ESJ Action Plan at 7.

¹⁸ *Id.* at 3-4.

¹⁹ D.88-12-083, 30 CPUC 2d 189, 221.

unnecessary costs. Based on the foregoing, we find that the Settlement Agreement is in the public interest.

3.1.5. Conclusion

As discussed above, the Settlement Agreement is reasonable in light of the whole record, consistent with the law, and in the public interest. In addition, the Settlement Agreement thoughtfully weighed other lower cost alternatives. If the alternative approach for the filter upgrades at the conventional facility is approved by DDW, the Project will cost \$22 million instead of the \$37.7 million²⁰ estimate included in the application. This would represent close to a \$15.7 million capital cost savings for customers. Therefore, this Settlement Agreement should be adopted by the Commission.

3.2. Review of Disputed Issues

3.2.1. Standard of Review

For the outstanding disputed issues San Gabriel bears the burden of proof to show that the regulatory relief it requests should be granted. The scoped issues that remained disputed and unresolved by the Settlement Agreement are: (1) whether San Gabriel should be authorized to apply AFUDC at its full rate of return while the Project is under construction and not yet used and useful; and (2) whether San Gabriel should be authorized to apply its full authorized rate of return for the post-in-service capitalized interest rate.²¹

²⁰ San Gabriel Application, January 29, 2021, at 6.

²¹ The post-in-service capitalized interest rate issue was introduced in the Joint Motion for Approval of Settlement Agreement filed September 27, 2021, but had not been included in the initial Scoping Memo dated July 12, 2021. The assigned Commissioner issued an Amended Scoping Memo on September 23, 2022, to include this issue in the scope.

3.2.2. AFUDC Interest Rate During Construction and Reasonableness of Project Funding Mechanisms

3.2.2.1. San Gabriel

San Gabriel, in its brief, recommended that the Commission authorize it to apply its authorized rate of return to company funds temporarily used to finance the Project. According to San Gabriel, this interest rate treatment is appropriate because it represents San Gabriel's overall cost of capital and would also have been the applicable rate if the Project was presented as a rate base project.²²

To support its position, San Gabriel asserted that, "... to the extent it is required to finance any unfunded portion of the Project, it will do so with a combination of internally generated cash flows (*i.e.*, equity) and long-term debt."²³ San Gabriel indicated that these are the same sources as any ordinary capital project.²⁴

San Gabriel claimed that the longstanding cost-of-service ratemaking and regulatory framework is one that provides the utility a reasonable opportunity to recover its cost of providing service, including the cost of capital deployed in the provision of such service, to the public.²⁵

San Gabriel stated that its acceptance of Contributions in Aid of Construction does not require a reduction in the rate of return authorized for the utility-funded portion of the Project.²⁶

²² Opening Brief of San Gabriel on Remaining Disputed Issues, October 11, 2021, at 7.

²³ *Ibid.*

²⁴ *Ibid.*

²⁵ *Ibid.*

²⁶ *Ibid.*

3.2.2.2. Cal Advocates

Cal Advocates, in its opening brief, recommended that the Commission reject San Gabriel's request to earn the authorized rate of return on funds temporarily used towards the Project.²⁷ Cal Advocates argued that the risk profile for the Project does not justify full rate of return treatment, and instead, the interest rate adopted for funds used during construction should be matched to the level of risk.²⁸ Cal Advocates noted San Gabriel's admission that its investment in this Project is not identical to the type of investment that would be included in rate base, and therefore, eligible for a full rate of return.²⁹

Cal Advocates maintained that because San Gabriel will be reimbursed by facilities fees for all temporary contributions it makes to fund to the Project, there is a much lower risk to the company than the typical rate base investment where the risk of regulatory disallowance may justify a full rate of return.³⁰ Cal Advocates emphasized its argument in its exhibit PAO-1 that, "... a return should be adequate to enable a utility to attract investors to finance the replacement and expansion of a utility's facilities to fulfill its public utility service obligations."³¹ Cal Advocates also asserted that, "... developer contributions provide an ongoing and dedicated source of Project funding."³²

The regulatory account that facilities fees are placed in earns interest at the 90-day commercial paper rate. Cal Advocates argued that San Gabriel should

²⁷ Opening Brief of Cal Advocates, October 11, 2021, at 3.

²⁸ *Id.* at 3-6.

²⁹ Exhibit SG-5 (J. Reiker Rebuttal Testimony) at 5.

³⁰ Opening Brief of Cal Advocates, October 11, 2021, at 4.

³¹ Exhibit PAO-1 at 2-25: 4-8.

³² Opening Brief of Cal Advocates, October 11, 2021, at 5.

not be permitted to earn a full rate of return (currently 8.12 percent) on temporary contributions to a lower risk investment while ratepayers earn a relatively low interest rate on the facilities fees that will be used to offset the Project costs.

Finally, Cal Advocates claimed that allowing San Gabriel to earn a full rate of return on temporary (financial) contributions to the Project may remove the incentive to manage the Project budget in a prudent manner. Cal Advocates suggested that the Commission treat company funds and developer funds in the same manner by applying the same interest rate to both sources of funds.³³

3.2.2.3. Conclusion

D.08-05-036 held that, "... the Commission should decide the interest rate treatment based upon the circumstances at hand and the type of financing being used to fund the Project."³⁴ The categorization of any project as a "capital project," does not automatically entitle a utility to receive AFUDC treatment at its authorized full rate of return. Therefore, in this case, the factual circumstances of the proposed Project and the level of risk the company is exposed to must be considered when determining AFUDC interest rate treatment.

San Gabriel's witness estimated that the entire cost of the Project will be funded by facilities fees in approximately four years.³⁵ However, San Gabriel in its application estimated that, assuming a rate of customer growth based on the more recent five-year period from 2014 to 2019, the entire cost of the Project will

³³ Opening Brief of Cal Advocates, October 11, 2021, at 6.

³⁴ D.08-05-036, Decision Determining Carrying Costs for Memorandum Account, May 29, 2008, at 11.

³⁵ Exhibit SG-3 at 10.

be funded (by facilities fees) in approximately three years.³⁶ Therefore, since this Project will be reimbursed by facilities fees in three to four years, it is not a typical long-term capital task requiring more risk and more generous interest rate treatment.

Cal Advocates noted the relatively low risk involved in the funding of the Project and argued that “... the return provided should be commensurate with the risk taken”³⁷ and argued that the AFUDC interest rate should be set at the 90-day commercial paper rate.

We agree with Cal Advocates that the funding for this Project involves relatively low risk. However, we disagree with Cal Advocates that the AFUDC rate should be set at the 90-day commercial paper rate as that rate would not compensate San Gabriel for the combination of short-term and long-term sources of funds it may use to support the Project.

Instead, we opine that the appropriate AFUDC interest rate for this Project lies between the 90-day commercial paper rate and the full rate of return for capital projects. San Gabriel should be authorized the interest rate that most closely reflects its level of risk and the actual rate it is likely to face, for short-term debt, during the expected period for Project completion. San Gabriel and other water companies operating in California should be encouraged to use facilities fees, as appropriate, to fund needed projects. Using facilities fees benefits customers since they do not increase rates.

³⁶ San Gabriel Application, January 29, 2021, at 28.

³⁷ Opening Brief of Cal Advocates, at 5.

This decision therefore sets the rate of interest accrued as AFUDC to be the then-current monthly cost for short-term debt.³⁸ This approach will compensate San Gabriel for its actual potential funding costs and, further, does not negatively impact its ratepayers. San Gabriel's proposed funding mechanisms for the Project are just and reasonable and in the ratepayer interest. San Gabriel's use of facilities fees is reasonable because this funding approach reduces the need to raise debt and equity capital, and ultimately customer rates.³⁹

3.2.3. Post-in-Service Capitalized Interest Rate

3.2.3.1. San Gabriel

Citing to D.08-05-036, San Gabriel's opening brief argued that regulatory compliance requirements (for water quality) and the long-term nature of the Project support authorizing full rate of return treatment for post-in-service capitalized interest for any capital project. San Gabriel maintained that the Commission should distinguish any capital contributions made to support the Project from the general facilities fees being collected from developers.⁴⁰

Moreover, San Gabriel asserted that the Project must go forward in some form and will require substantial investment.⁴¹ According to San Gabriel, the established ratemaking treatment for capital projects also supports applying the authorized rate of return for post-in-service capitalized interest.⁴²

³⁸ This means that San Gabriel should use whatever financial instruments it would use for short-term debt in compliance with its cost of capital authorizations.

³⁹ San Gabriel Application, January 29, 2021, at 26.

⁴⁰ Opening Brief of San Gabriel on Remaining Disputed Issues, October 11, 2021, at 10.

⁴¹ *Ibid.*

⁴² *Id.* at 9.

3.2.3.2. Cal Advocates

Cal Advocates' opening brief argued that it is inappropriate for San Gabriel to earn a full rate of return once the Project is completed and placed into service. According to Cal Advocates, if the Commission authorizes full rate of return treatment, San Gabriel will receive approximately ten times the rate that developers (and, therefore, ratepayers) receive on financial contributions to the same account.⁴³ Pointing to the low level of financial risk that San Gabriel will experience for this Project, Cal Advocates reiterated the concept that the return should be commensurate with the risk taken.⁴⁴

3.2.3.3. Conclusion

San Gabriel's supply of funds for this Project, whether during construction or post-in-service, is to address the timing mismatch between the use of capital in designing and constructing the Project and the source of capital for the Project from the facilities fees. Whether during construction or post-in-service, the supply of funds that may be provided by San Gabriel is analogous to a short-term bridge loan that will be paid off as facilities fees accumulate. As in Section 3.2.2.3, we rely on D.08-05-036, which held that, "... the Commission should decide the interest rate treatment based upon the circumstances at hand and the type of financing being used to fund the Project."⁴⁵ This decision therefore sets the rate of interest for post-in-service expenses to be the then-current monthly cost for short-term debt.⁴⁶

⁴³ Opening Brief of Cal Advocates, October 11, 2021, at 7.

⁴⁴ *Id.* at 5.

⁴⁵ D.08-05-036, Decision Determining Carrying Costs for Memorandum Account, May 29, 2008, at 11.

⁴⁶ This means that San Gabriel should use whatever financial instruments it would use for short-term debt in compliance with its cost of capital authorizations.

In taking the same approach here as for AFUDC, we allow San Gabriel to benefit from carrying costs commensurate with the risk related to the Project in the instant application.

4. Comments on Proposed Decision

The Proposed Decision in this matter was mailed to the Parties in accordance with Public Utilities Code Section 311 and comments were allowed under Rule 14.3. Comments were filed on _____ by _____. Reply comments were filed on _____ by _____.

5. Assignment of Proceeding

Genevieve Shiroma is the assigned Commissioner and Hazlyn C. Fortune is the assigned ALJ in this proceeding.

Findings of Fact

1. On January 29, 2021, San Gabriel filed A.21-01-017 requesting authority to apply facilities fees to fund upgrades for water treatment facilities in the Project.
2. On March 3, 2021, Cal Advocates filed a protest to A.21-01-017.
3. On September 27, 2021, Parties filed a Joint Motion for Approval of the Settlement Agreement and a separate motion to move exhibits into evidence.
4. The Settlement Agreement resolves all but two of the issues identified in the scope of this proceeding: (1) whether San Gabriel should be authorized to apply AFUDC at its full rate of return while the Project is under construction and not yet used and useful; and (2) whether San Gabriel should be authorized to apply its full authorized rate of return for the post-in-service capitalized interest rate.

5. Adoption of the Settlement Agreement is in the public interest because customer rates will not increase with the use of facilities fees to fund the Project and the Project will improve water quality.

6. Facilities fees represent an ongoing and dedicated source of Project funding.

7. Facilities fees are placed in an account that earns interest at the 90-day commercial paper rate.

8. San Gabriel's current rate of return is 8.12 percent.

9. Using facilities fees to offset the cost of the Project entails less risk than other financial funding options.

10. D.08-05-036 found that interest rate treatment should be based on the circumstances at hand and the type of financing being used to fund a project.

Conclusions of Law

1. San Gabriel should be authorized to use facilities fees to offset the costs for Project upgrades at Fontana.

2. The Joint Motion, filed on September 27, 2021, for adoption of the Settlement Agreement complies with Article 12 of the Commission's Rules of Practice and Procedure and should be granted.

3. The Settlement Agreement (attached to this decision as Attachment A) is reasonable in light of the whole record, consistent with law, and in the public interest and should be adopted.

4. The Parties have complied with the provisions of Rule 12.1.

5. Pursuant to Rule 12.5, the Settlement Agreement does not bind or otherwise impose a precedent in this or any future proceeding.

6. It is reasonable to use D.08-05-036 to guide pre- and post-construction interest rate treatment based on the actual financing circumstances at hand.

7. San Gabriel should be authorized to use its then current monthly cost for short-term debt during the Project construction and post-in-service periods.

8. It is reasonable to make Project costs subject to a reasonableness review in San Gabriel's next GRC.

9. The design and construction costs of the Project and any accrued capitalized interest costs should be recorded in a separately identified Project Work Order.

10. San Gabriel should offset all Project costs and any accrued capitalized interest costs recorded in the Project Work Order by the amounts of facilities fees received pursuant to Fontana Tariff Schedule No. FO-FF.

11. San Gabriel should not record or include any Project costs or accrued capitalized interest costs in its rate base or revenue requirement for ratemaking purposes.

12. San Gabriel should record facilities fees and grants and contributions from other sources received to offset Project costs and accrued capitalized interest costs as contributions in aid of construction.

O R D E R

IT IS ORDERED that:

1. The Joint Motion, filed on September 27, 2021, for adoption of the Settlement Agreement is granted.

2. The Settlement Agreement between San Gabriel Valley Water Company and the Public Advocates Office of the California Public Utilities Commission, attached hereto as Attachment A, is approved and adopted.

3. San Gabriel Valley Water Company shall record, in a separately identified Project Work Order, the design and construction costs of the Summit Treatment Plant covered by Application 21-01-017 and any accrued capitalized interest costs.

4. San Gabriel Valley Water Company shall record facilities fees, grants and contributions from other sources received to offset Summit Treatment Plant costs and accrued capitalized interest costs as contributions in aid of construction.

5. San Gabriel Valley Water Company shall offset all Summit Treatment Plant costs and any accrued capitalized interest costs recorded in the Project Work Order by the amounts of facilities fees received pursuant to Fontana Tariff Schedule No. FO-FF and any other financial contributions until all the Summit Treatment Plant costs and any accrued capitalized interest costs have been offset and reimbursed.

6. San Gabriel Valley Water Company shall record the cost of funding of Project costs and any capitalized interest costs as an allowance for funds used during construction on the unreimbursed balance, if any, in the Project Work Order until all the Summit Treatment Plant costs are offset and reimbursed.

7. San Gabriel shall not record or include any Summit Treatment Plant costs or accrued capitalized interest costs and in its rate base or revenue requirement for ratemaking purposes.

8. All Summit Treatment Plant costs shall be subject to a reasonableness review in the San Gabriel Valley Water Company's next general rate case.

9. The joint motion, filed on September 27, 2021, to receive exhibits into evidence is granted.

10. Application 21-01-017 is closed.

This order is effective today.

Dated _____, at San Francisco, California.

ATTACHMENT A

**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**

Application of SAN GABRIEL VALLEY
WATER COMPANY (U337W) for Authority
to Apply Facilities Fees to Fund Upgrades to
Water Treatment Facilities in the Fontana
Water Company Division.

A.21-01-017
Filed January 29, 2021

**SETTLEMENT AGREEMENT
BETWEEN SAN GABRIEL VALLEY WATER COMPANY
AND THE PUBLIC ADVOCATES OFFICE**

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September 27, 2021

**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**

Application of SAN GABRIEL VALLEY
WATER COMPANY (U337W) for Authority
to Apply Facilities Fees to Fund Upgrades to
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A.21-01-017
Filed January 29, 2021

**SETTLEMENT AGREEMENT
BETWEEN SAN GABRIEL VALLEY WATER COMPANY
AND THE PUBLIC ADVOCATES OFFICE**

I. GENERAL PROVISIONS

1. Pursuant to Article 12 of the Rules of Practice and Procedure (“Rules”) of the California Public Utilities Commission (“Commission”), the Public Advocates Office at the Public Utilities Commission (“Cal Advocates”) and San Gabriel Valley Water Company (“San Gabriel”) (collectively, “the Parties,”) have agreed on the terms of this Settlement Agreement, which they now submit for the Commission’s review and consideration. This Settlement Agreement addresses most of the disputed issues between San Gabriel and Cal Advocates and, by extension, related derivative issues. The Parties respectfully request that the Commission approve the Settlement Agreement as submitted.

2. The issues that the Parties agree to resolve through this Settlement Agreement are set forth in Section II below. Section II describes the positions of the Parties and the resolution provided by the Settlement Agreement.

3. Because this Settlement Agreement represents a compromise of the Parties’ positions with respect to each issue addressed herein, the Parties have agreed upon the resolution of each issue addressed in the Settlement Agreement on the basis that its approval by the Commission should not be construed as an admission or concession by any Party regarding any fact or matter of law that may be in dispute in this proceeding. Furthermore, consistent with Rule 12.5 of the Rules, the Parties intend that the approval of this Settlement Agreement by the Commission should not be construed as a precedent or statement of policy of any kind for or against any Party in any current or future proceeding with respect to any issue addressed in the Settlement Agreement.

4. The Parties agree that no signatory to the Settlement Agreement assumes any personal liability as a result of his or her execution of this document. All rights and remedies of the Parties are limited to those available before the Commission.

5. This Settlement Agreement may be executed in counterparts, each of which shall be deemed an original, and the counterparts together shall constitute one and the same instrument.

6. This Settlement Agreement constitutes and represents the entire agreement between the Parties and supersedes all prior and contemporaneous agreements, negotiations, representations, warranties and understandings of the Parties with respect to the subject matter set forth herein.

7. If after approval by the Commission, one Party fails to perform its respective obligations under this Settlement Agreement, the other Party may come before the Commission to pursue a remedy, including enforcement.

8. The Parties agree that this Settlement Agreement is an integrated agreement, and the provisions of the Agreement are not severable. Therefore, if the Commission rejects, conditions, or modifies any term or portion of this Settlement Agreement, the Parties shall convene a conference within fifteen days thereof and engage in good faith negotiations to determine whether some or all of the remainder of the Settlement Agreement is acceptable to the Parties. In the event an agreement is reached, both Parties must consent in writing to any changes or the Settlement Agreement is void. If the Parties cannot agree to resolve any issue raised by the Commission's actions within thirty days of their conference, this Settlement Agreement shall be rescinded, the Parties shall be released from any obligation, representation, or condition set forth in this Settlement Agreement, including their obligation to support this Settlement Agreement, and the Parties shall be restored to their positions prior to having entered into this Settlement Agreement. Thereafter, the Parties may pursue any action they deem appropriate.

9. The Parties agree that this Settlement Agreement shall be governed by the laws of the State of California as to all matters, including validity, construction, effect, performance, and remedy.

10. This resolution of the issues addressed by this Settlement Agreement is supported by the Parties' respective prepared testimony and reports, identified as follows:

Exhibit	Title
SG-1	<i>Direct Testimony of Josh M. Swift</i> (Served on January 29, 2021)
SG-2	<i>Direct Testimony of Matt Y. Yucelen</i> (Served on January 29, 2021)
SG-3	<i>Direct Testimony of Joel M. Reiker</i> (Served on January 29, 2021)
SG-4	<i>Rebuttal Testimony of Josh M. Swift</i> (Served on August 6, 2021)
SG-5	<i>Rebuttal Testimony of Joel M. Reiker</i> (Served on August 6, 2021)
PAO-1	<i>Report on San Gabriel Valley Water Company's Request for Authority to Apply Facilities Fees to Fund Upgrades to Water Treatment Facilities in the Fontana Water Division</i> (Served on July 23, 2021)

11. There remain contested issues between the Parties that are unresolved under this Settlement Agreement. The Parties will brief the following issues for resolution by the Commission:

- Whether San Gabriel should be authorized to apply its full authorized rate of return for the Allowance for Funds Used During Construction (“AFUDC”) rate while the project is under construction and not yet used and useful?
- Whether San Gabriel should be authorized to apply its full authorized rate of return for the post-in-service capitalized interest rate for the project?

II. RESOLUTION OF DISPUTED ISSUES

A. San Gabriel’s Position on Disputed Issues

San Gabriel proposed modifications to the Summit Water Treatment Plant (“Summit Plant”) that comprise the Project proposed in A.21-01-017, which includes decommissioning and retiring the existing outdated Sandhill Diatomaceous Earth (“DE”) filtration facility, adding two filters to the Conventional Treatment facility, increasing the amount of filter media in each filter, and adding granular activated carbon (“GAC”) contactors.

After investigation and numerous studies, San Gabriel has concluded that treated water from its Summit Plant is at significant risk of exceeding U.S. EPA’s Stage II Disinfection By-Products Rule in its distribution system. In addition, San Gabriel has concluded that the Summit Plant’s existing treatment systems are ineffective at removing seasonal taste and odor compounds from source water supplied from Silverwood Lake, a terminal reservoir of the State Water Project, which results in customer complaints. Finally, San Gabriel has concluded that retirement of the outdated DE filtration facility requires optimizing filter operations by increasing the maximum allowable filtration rate approved by Division of Drinking Water (“DDW”).

B. Cal Advocates’ Position on Disputed Issues

Cal Advocates recommended that San Gabriel conduct pilot tests, including to re-rate filters for full-scale testing of filtration rates and pilot testing of filter absorbers for taste and odor removal, prior to proceeding with any modifications at the Summit Plant.

Cal Advocates further recommended that San Gabriel, after completing pilot studies, proceed with certain modifications including the installation of the two new filters at the Conventional Treatment facility and adding GAC to the existing filters, instead of the proposed post-filter GAC contactors at the Conventional Treatment plant.

Cal Advocates did not oppose San Gabriel’s use of Facilities Fees to fund the Summit plant project, but did oppose granting San Gabriel a full rate of return to any investor funds used towards the project and instead recommended that the 90-day commercial paper rate be applied.

C. Resolution of Disputed Issues

These Settlement Agreement terms represent a compromise of the Parties' positions. Approval of this Settlement Agreement by the Commission will authorize the following:

- 1) Design, permitting, and construction of two new filters, including extension of the existing filter gallery, associated piping, chemical related facilities, and control system upgrades to the Conventional Treatment facility.

- 2) Decommissioning and removal of the outdated DE filtration facility.

The estimated combined cost for Items 1 and 2 is: \$20,000,000.

- 3) Modification of the Summit Plant's 5 filters (3 existing filters and 2 newly constructed filters) by replacing the dual media (anthracite coal and sand) with GAC only if the following conditions are met:

- a. Under the direction of the DDW, San Gabriel will perform pilot scale testing to evaluate the feasibility and operational efficiency of replacing Summit Plant's existing dual filter media (anthracite coal and sand) with GAC.
- b. The objectives of the tests are to evaluate feasibility of operating and maintaining Summit Plant's 5 filters with GAC filter media, confirm reduction of disinfection by-product precursors in compliance with DDW regulations, determine the optimum GAC filter media depth and allowable filtration rate above 6 gpm/ft², evaluate the effectiveness of GAC filter media to remove taste and odor compounds and the ability to meet all state and federal surface water drinking standards.
- c. Upon successful completion of testing and review and approval by DDW, replace the dual filter media in each of the 5 filters with GAC, and make other necessary modifications to the existing filters as required by DDW.
- d. The estimated cost for Item 3 is: \$2,000,000.

- 4) If after completion of the pilot tests, DDW does not approve the treatment modification to retrofit Summit Plant's existing 5 filters with GAC, San Gabriel shall file a Tier 1 advice letter to change the scope of the Project to include the construction of 6 GAC contactors, low lift booster pumping station, associated piping, and equipment, and to provide an updated cost estimate for the project. The estimated cost for Item 4 is \$18,000,000. San Gabriel must provide copies of documents and communications with DDW relating to the Project to Cal Advocates as these documents are produced and available. San Gabriel must also provide the most recent DDW Disinfection Byproducts reports showing San Gabriel's water quality in the distribution system. Cal Advocates reserves the right to protest San Gabriel's advice letter to change the scope of the Project

if adequate support is not provided or if there is a significant increase in the estimated costs.

- 5) **Annual Submission of Advice Letters:** In order for Cal Advocates, Water Division, and the Commission to stay abreast of San Gabriel’s progress on the design and construction of the Project and to be in a better position to conduct a reasonableness and prudence review of the actual construction costs in a future General Rate Case (“GRC”) after the Project is completed and placed in service, San Gabriel shall submit a Tier 1 advice letter on or before March 31 of each year until the project is completed and placed in service. Cal Advocates reserves its right to conduct discovery related to the Tier 1 advice letter and to protest the advice letter. Each Tier 1 advice letter shall include the following:
 - a. Ongoing Project construction costs incurred through the most recently-closed accounting period (for a March 31 advice letter submission date, this will be December 31 of the previous calendar year). The job cost worksheets itemizing the individual charges to the work order, including a description of the charge (i.e. payroll, AP vendor invoice, etc.) shall be provided as supporting workpapers. To the extent any AFUDC or post-in service capitalized interest is recorded in the Project work order on any balance of project costs not covered by Facilities Fees in any given month, San Gabriel shall provide detailed workpapers showing the calculation of the AFUDC/post-in service capitalized interest.
 - b. The amount of Facilities Fees collected and applied to the Project through the most recently-closed accounting period. A copy of the Facilities Fee Memorandum Account showing Facilities Fees collected, Facilities Fees applied to the Project, the applicable commercial paper rate, and interest recorded in the memorandum account shall be provided as a supporting workpaper.
 - c. A detailed discussion/explanation addressing the following:
 - i. Percentage of completion for each stage/component of the project (e.g. design, construction of additional filters, pilot testing, etc.).
 - ii. How the recorded costs for each stage/component of the project compare to San Gabriel’s original estimated cost, based on the percentage of completion.
 - iii. To the extent there is any variance between the recorded costs for a given stage/component of the Project and San Gabriel’s original estimated cost, San Gabriel shall provide a detailed explanation and justification of the variance with supporting documentation, as applicable.
- 6) **General Rate Case Reasonableness and Prudence Review:** San Gabriel commits to exclude the capital costs of the Project from rate base. No Project costs, including AFUDC and post-in service capitalized interest related to the Project, will ever be included in San Gabriel’s rate base or become the responsibility of residential customers for ratemaking purposes.

- a. In the first GRC San Gabriel submits after the Project is completed and placed in service, San Gabriel shall provide details of all Project costs, broken down by stage/component, along with the amount of Facilities Fees applied. San Gabriel shall also address the following:
 - i. Total Project costs compared to San Gabriel's original estimated Project costs, with an explanation and justification of any variances between the two.
 - ii. An explanation/discussion of any AFUDC and/or post-in service capitalized interest recorded in the Project work order, with supporting calculations and documentation.
- b. To the extent any balance of final Project costs remains unfunded by Facilities Fees after the Project is completed and placed in service, such balance shall be excluded from Utility Plant in Service (and thus excluded from customer rates) until such balance (including post-in service capitalized interest) is completely offset by Facilities Fees recorded as Contributions in Aid of Construction.
- c. To the extent the Project is not completed, and thus remains under construction at the time San Gabriel files its next GRC, the balance of costs recorded in the Project work order shall be excluded from the amount of Construction Work in Progress that is included in rate base and in no event shall be used for estimating the future Construction Work in Progress amounts that are used to develop revenue requirement.
- d. In the first GRC San Gabriel submits after the Project is completed and placed in service, Cal Advocates reserves the right to challenge the prudence of the Project and the reasonableness of the Project costs. The parties will not ask the Commission to limit its authority, to the extent the Commission finds any portion of the Project or costs thereof to be unreasonable or imprudent, to exclude such portion from the balance of Utility Plant in Service, and re-assign an equivalent amount of Facilities Fees from Contributions in Aid of Construction back to the Facilities Fee memorandum account for future use as approved by the Commission.

7) **Application of Facility Fees to fund upgrades to the Summit Plant:**

- a. San Gabriel shall record the costs of planning, designing and constructing the Project in a separate project work order;
- b. San Gabriel will offset all such recorded Project costs with the amount of Facilities Fees San Gabriel collects pursuant to Fontana Water Company division Tariff Schedule No. FO-FF until all of the Project costs have been offset and reimbursed, including the cost of San Gabriel's funding of the Project recorded as

an allowance for funds used during construction (AFUDC) on the unreimbursed balance during construction, if any, and post-in service capitalized interest on the unreimbursed balance after the Project is completed and placed in service, if any, until all of the Project costs are offset and reimbursed by Facilities Fees.

- c. The Parties will litigate and the Commission will determine in this proceeding which AFUDC rate to be applied to any unfunded balance during construction, if any. The post-in service capitalized interest rate on any unreimbursed balance after the Project is completed and placed in service, if any, shall also be litigated and determined by the Commission in this proceeding.
- d. All such Facilities Fees, as well as any grants or other contributions received to offset the Project costs, shall be recorded as contributions in aid of construction.

III. CONCLUSION

1. The Parties mutually believe that, based on the terms and conditions set forth above, this Settlement Agreement is reasonable, consistent with the law, and in the public interest.
2. Each Party to this Settlement Agreement represents that his or her signature to this Settlement Agreement binds his or her respective party to the terms of this Settlement Agreement.

Respectfully submitted,

Respectfully submitted,

THE PUBLIC ADVOCATES OFFICE

SAN GABRIEL VALLEY WATER
COMPANY

By: Chris Ungson
Chris Ungson
Deputy Director

By: _____
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Dated: September 27, 2021

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(END OF ATTACHMENT A)